

**PUBLIC UTILITY COMMISSION OF OREGON
STAFF REPORT
PUBLIC MEETING DATE: July 12, 2022**

REGULAR CONSENT EFFECTIVE DATE _____ N/A _____

DATE: July 1, 2022

TO: Public Utility Commission

FROM: Brian Fjeldheim

THROUGH: Bryan Conway, Marc Hellman, and Matt Muldoon **SIGNED**

SUBJECT: NORTHWEST NATURAL:
(Docket No. UM 903)
2022 Spring Earnings Review.

STAFF RECOMMENDATION:

Staff recommends the Public Utility Commission of Oregon (Commission) accept Staff's finding that Northwest Natural Gas Company's (NW Natural or Company) earnings for the 12 months ended December 31, 2021, are below the earnings threshold established in Docket No. UM 903, and that no Earnings Sharing applies to the 2021 Fiscal Year.

DISCUSSION:

Issue

Whether the Commission should approve Staff's finding that NW Natural's earnings for the 12 months ended December 31, 2021, are below the earnings threshold established in Docket No. UM 903, and that no Earnings Sharing applies to the 2021 Fiscal Year.

Applicable Rule or Law

NW Natural made its filing in accordance with OAR 860-022-0070. Each Oregon regulated natural gas distribution company recovers gas costs under an automatic adjustment clause known as the Purchased Gas Adjustment (PGA). The Commission adopted the PGA in 1998 and the implementing rules in 1999.¹ The Commission has modified the PGAs and rules through the years.² The purpose of the PGA is to permit

¹ Order Nos. 98-503 and 99-272 (Docket Nos. UM 903 and AR 357).

² See e.g., Order Nos. 07-019 and 08-504 (Docket Nos. AR 512 and UM 1286).

each natural gas utility to adjust revenue annually to reflect actual increases or decreases in gas costs.

The PGA has two components. The first component is prospective and resets base gas costs each year to reflect changes in the utility's cost of purchased gas.³ The second component is retroactive and allows the utility to defer for later inclusion in rates differences between actual fixed costs and the base level in rates as well as a portion of the differences between actual commodity-related costs and the base level in rates.⁴

To ensure that earnings of a natural gas utility are not excessive prior to passing through prudently incurred base gas costs, the Commission, by rule (OAR 860-022-0070), requires that an earnings review be conducted on an annual basis.⁵

Components of the Spring Earnings Review are as follows:

Annual Election

Not later than September 15 of each year, each Local Distribution Company (LDC) must make an annual sharing election for the applicable gas year, which begins November 1.⁶ The LDC must choose either 90/10 Weighted Average Cost of Gas (WACOG) sharing or 80/20 WACOG sharing with a corresponding earnings review threshold.⁷

Spring Earnings Review

An earnings review shall be performed each spring (pursuant to OAR 860-022-0070) based on the most recent fiscal year's results of operations. The earnings review will apply to the WACOG sharing election previously made by the Company (e.g., the 2020 election will apply to the 2021 Fiscal Year results of operations that are the subject of the 2022 Spring Earnings Review). If earnings are found to be above a specified return on equity (ROE) level (Earnings Threshold), a portion of those revenues will be booked to a deferred account.

³ See e.g., Order No. 03-198 at 1 (Docket No. AR 449).

⁴ Id.

⁵ Id.

⁶ Order No. 08-504 at 17; Order No. 11-196, Appendix at 4; Order No. 14-238, Appendix A at 8.

⁷ 90/10 or 80/20 WACOG Sharing means that 90 or 80 percent of the variance will be deferred for subsequent charge or credit to customers, and 10 or 20 percent will be absorbed or retained by the LDC.

The Earnings Threshold

An LDC that elects 90/10 WACOG sharing will be subject to an Earnings Threshold of 100 basis points above its ROE, adjusted to reflect changes in conditions in capital markets.⁸ An LDC that elects 80/20 WACOG sharing is subject to an Earnings Threshold of 150 basis points above its ROE, adjusted in the same manner.⁹

Structure of Earnings Reviews

By May 1 of each year, the LDC will file results of operations for the 12 months ended the prior December 31. Staff will complete its review and distribute summary conclusions by June 10 to all parties. At the first regular public meeting in July, Staff will present the results of the earnings review. If there are unresolved issues, a settlement conference will be held. If there are still outstanding issues, parties will file position statements by August 1 and the Commission would issue its decision on unresolved issues by August 15. These rate changes will include amortization of credit amounts in the deferred account, if any, resulting from the spring earnings review.¹⁰

Earnings Adjustments

Recorded results of operations will include retained WACOG variance earnings and will be adjusted for Type 1 adjustments as set forth in Order No. 99-272, Appendix B. NW Natural made a one-time election to include a weather normalization adjustment in its spring 1999 earnings review filing and each subsequent annual filing.

Earnings Performance

If adjusted earnings (including any retained WACOG variance) are below the Earnings Threshold, there will be no rate adjustment.¹¹ If adjusted earnings are above the Earnings Threshold, the amount of revenue in the test year representing 33 percent of the earnings (including WACOG earnings) exceeding the threshold will be shared with customers (Earnings Sharing).¹²

Effective Date of Rate Adjustment and Applicable Interest

Upon completion of the earnings review, any amount of earnings over the sharing dead band determined to be returned to customers will be booked to a deferred account. Interest shall apply beginning the previous January 1. The rate adjustment and amortization will be effective with the date of the subsequent base gas cost change.¹³

⁸ The Earnings Threshold is adjusted each year by 20 percent of any change in the risk-free rate for the twelve-month calendar year preceding the annual earnings review (See Order No. 04-203 at 3-4 and OAR 860-022-0070(5)(c)).

⁹ Id.

¹⁰ OAR 860-022-0070(6).

¹¹ OAR 860-022-0070(5)(c).

¹² Order No. 98-543.

¹³ OAR 860-022-0070(5)(e).

Analysis

NW Natural's Earnings

The Gas Earnings Threshold (GET) for NW Natural for this 2022 Spring Earnings review (review of the 2021 results of operations) is 10.50 percent.¹⁴ NW Natural elected a 90/10 WACOG sharing for the 2021 Fiscal Year in Docket No. UM 1286.¹⁵ Accordingly, the calculation of NW Natural's Earnings Threshold began with the Company's authorized ROE for 2021.¹⁶ Then 100 basis points (based on a 90/10 WACOG Sharing Election) were added to NW Natural's ROE. Finally, an adjustment of 20 percent of the change in United States Treasury Risk Free Rate for the twelve-month period preceding the annual earnings review and the Company's most recent general rate case order was applied. For the 2021 Fiscal Year, NW Natural's adjusted risk-free rate increased 10 basis points.

Pursuant to OAR 860-022-0070, NW Natural submitted its 2021 Results of Operations (ROO) report for the 12 months ended December 31, 2021.¹⁷ NW Natural calculates its ROE as 8.68 percent after the application of its Type 1 adjustments, including weather normalization.

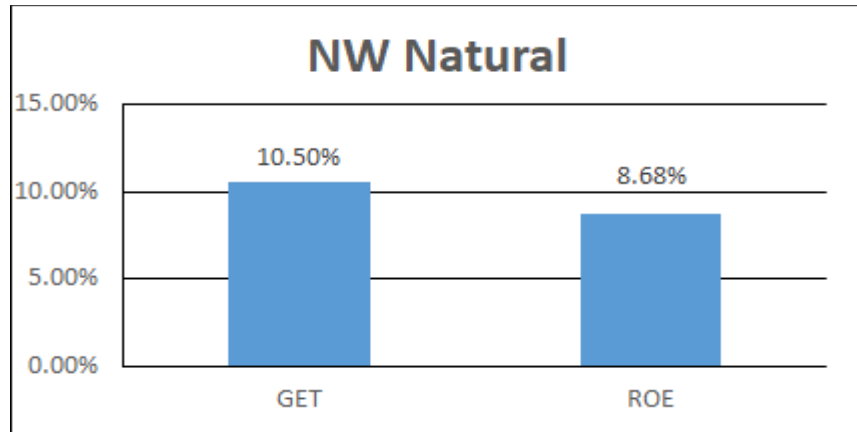
Staff reviewed NW Natural's ROO report and the supporting workpapers and concludes that NW Natural's reported ROE has been calculated correctly. Because NW Natural's adjusted ROE is below the GET of 10.50 percent, no Earnings Sharing is required.

¹⁴ Gas Earning Thresholds and supporting calculations are posted on the Commission's website here: <https://www.oregon.gov/puc/forms/Forms%20and%20Reports/Gas-Earnings-Threshold-GET.pdf>.

¹⁵ Company's Annual PGA Sharing Election (2020-2021), Docket No. UM 1286 filed September 15, 2020.

¹⁶ NW Natural's 2021 authorized ROE is 9.40 percent, per Docket No. UG 344, Order No. 18-419 at page 4; and Docket No. UG 388, Order No. 20-369 at page 3.

¹⁷ *In the Matter of Northwest Natural Gas Company dba NW Natural, Annual Earnings Review Report - Results of Operations*, Docket No. RG 40, submitted April 30, 2021.



OAR 860-022-0070(6) requires Staff to submit its conclusions to parties by June 10. Due to heavy workload, Staff submitted its conclusions to the parties in Docket No. UM 903 on July 5, 2022. Staff is unaware of any unresolved issues following its presentation of this review to the parties.

Conclusion

Staff reports above its calculations of: (1) the Company's adjusted return on equity ("Earnings Threshold"), and (2) adjusted revenues for the 2021 Fiscal Year, both of which are used to determine whether NW Natural must share a portion of its 2021 Fiscal Year earnings with customers under NW Natural's PGA mechanism. Based on these calculations, Staff concludes that NW Natural should not be required to share its 2021 earnings with customers in connection with its PGA.

PROPOSED COMMISSION MOTION:

Accept Staff's finding that NW Natural's 2021 earnings are below the Earnings Threshold designated in Docket No. UM 903, and that no Earnings Sharing applies to the 2021 Fiscal Year.